

GAO

Report to the Ranking Minority
Member, Committee on Small Business
and Entrepreneurship, U.S. Senate

October 2001

SMALL BUSINESS

HUBZone Program Suffers From Reporting and Implementation Difficulties

DISTRIBUTION STATEMENT A:
Approved for Public Release -
Distribution Unlimited

20011205 042



GAO

Accountability * Integrity * Reliability



GAO

Accountability * Integrity * Reliability

United States General Accounting Office
Washington, DC 20548

October 26, 2001

The Honorable Christopher S. Bond
Ranking Minority Member
Committee on Small Business and Entrepreneurship
United States Senate

Dear Senator Bond:

The Congress created the Historically Underutilized Business Zone (HUBZone) program to stimulate economic development and create jobs in distressed urban and rural areas, called HUBZones. To achieve these goals, the HUBZone program provides more access to federal contracting opportunities for small businesses. The Small Business Administration (SBA) administers the program, and federal agencies report their program achievements—the number and value of contract awards—to the Federal Procurement Data Center (FPDC). In fiscal year 2000, federal agencies reported awarding \$663 million in contracts under the HUBZone program. In response to your request, we examined (1) whether HUBZone program achievements are being accurately reported, and if not, the reasons for inaccuracies and (2) whether federal agencies are having difficulty implementing the HUBZone program to award contracts to certified HUBZone firms, and if so, the reasons for the difficulty.

Results in Brief

Reported HUBZone program achievements for fiscal year 2000 were significantly inaccurate. We found that the value of contracts awarded to HUBZone firms could be hundreds of millions of dollars different than the reported achievements. The federal agencies' data (1) included contracts awarded to firms that SBA had not certified as qualified to participate in the program, (2) included contracts awarded before the HUBZone program began in March 1999, and (3) did not include contracts awarded to firms that SBA may have certified as qualified HUBZone firms. We could not conclusively determine actual HUBZone program achievements because of these inaccuracies. The inaccuracies resulted from data entry errors and insufficient guidance on how to report agency data. FPDC includes the inaccurate data in its annual report on federal procurement activities. As a result of data problems, the Congress and federal agencies cannot use this data to gauge the program's success or to ensure that the program is working as intended.

After interviewing contracting officials and analyzing FPDC and SBA information, we concluded that federal agencies are having difficulties implementing the HUBZone program. Federal agencies did not achieve the fiscal year 2000 participation goal of 1.5 percent of the value of all prime contract awards. Further, federal agencies obligated only \$24 million to HUBZone firms as a result of applying the provisions of the HUBZone Act.¹ The primary reasons that federal contracting personnel gave for not using the HUBZone program to award contracts were: (1) the small number of SBA certified HUBZone firms, (2) difficulty identifying certified firms with the capabilities needed by federal agencies, (3) SBA's guidance that emphasizes the 8(a) program² over the HUBZone program, and (4) easier and quicker procedures to award contracts under the 8(a) program.

We are making recommendations to the Office of Federal Procurement Policy and SBA concerning the need to more accurately report the achievements under the HUBZone program and for additional and clarified guidance on how to more effectively locate certified HUBZone firms with capabilities that meet agencies' needs. In commenting on a draft of this report, SBA and the Office of Federal Procurement Policy generally agreed with our findings and provided clarifying suggestions for two recommendations, which we incorporated. SBA did express a concern about our characterization of SBA's emphasis on the 8(a) program. We believe our report accurately reflects the policies in effect at the time of our review and acknowledges the changes initiated by SBA. SBA's written comments appear in appendix II.

Background

The Historically Underutilized Business Zone (HUBZone) Act of 1997 established a program to provide assistance in securing federal contracts to small businesses located in HUBZones. HUBZones are metropolitan area census tracts or nonmetropolitan counties in which low-income levels or high unemployment rates qualify them as economically distressed. Also, all federally-recognized Indian reservations are HUBZones. The purpose of the HUBZone program is to increase employment opportunities, investment, and economic development in these areas.

¹ Title VI of the Small Business Reauthorization Act of 1997 (P.L. 105-135).

² The 8(a) program, also administered by the SBA, is one of the federal government's vehicles for developing small businesses that are owned by socially and economically disadvantaged individuals.

The HUBZone Act established (1) eligibility requirements that firms must meet to participate in the program, (2) contracting preferences that federal agencies can use to award contracts to firms certified by SBA as qualified HUBZone firms, and (3) goals for program participation by HUBZone firms as a percent of the total value of prime contract awards. The act identified ten federal agencies for initial participation in the program through the end of fiscal year 2000, and three more agencies were added in November 1999. (See appendix I for a list of the 13 agencies.) Currently, the HUBZone program applies to all federal agencies.³

SBA must certify that a firm qualifies for participation before federal agencies can award a contract under the program. To be qualified, the firm must apply with SBA and meet the following requirements:

- The firm must be a small business owned and controlled by one or more U.S. citizens.⁴
- The firm's principal office must be located in a HUBZone.
- Finally, at least 35 percent of the firm's employees must reside in a HUBZone.

Once SBA has certified that a firm is qualified, SBA adds the firm's name, address and certification date to its List of Qualified HUBZone Small Business Concerns maintained on SBA's World Wide Web site. In addition, SBA adds this certification to the firm's profile in SBA's on-line PRO-Net database, which contains information supplied by over 200,000 small businesses. SBA's list and PRO-Net are federal contracting officers' primary information sources for determining a firm's eligibility under the HUBZone program.

To increase employment and encourage economic development in areas designated as HUBZones, federal agencies can use any of three preferences specified in the HUBZone Act when awarding contracts to certified small businesses, as follows:

³ 13 CFR part 126.101.

⁴ The HUBZones in Native America Act of 2000 (P.L. 106-554, Title VI), among other things, expanded the definition of HUBZone small business ownership and control to include Alaska Native Corporations, Indian tribal governments, and community development corporations, and more precisely defined the term "Indian reservation".

-
- First, a contracting officer can give a HUBZone firm a price evaluation preference when participating in a full and open competition. In these cases, the contracting officer can deem the price offered by the HUBZone firm as lower than a price offered by another firm if (1) the other firm is not a small business and (2) the HUBZone firm's offered price is not more than 10 percent higher than the otherwise lowest price.
 - Second, a contracting officer can set aside a contract for competition only among certified HUBZone firms if two or more responsible HUBZone firms are expected to submit offers and the agency can award the contract at a fair market price.⁵
 - Finally, a contracting officer can award a sole source contract to a HUBZone firm if the officer determines among other things that two or more responsible HUBZone firms are not likely to submit offers and the agency can award the contract at a fair and reasonable price.

The HUBZone Act established participation goals for certified firms starting with fiscal year 1999. The fiscal year 1999 goal was 1 percent of the year's total value of prime contract awards, and the fiscal year 2000 goal was 1.5 percent. The act increased the goal by one-half percent each year, reaching 3 percent in fiscal year 2003 and each fiscal year thereafter. Because of delays in HUBZone program implementation, fiscal year 2000 was the first year agencies reported data to FPDC. Under the Small Business Act, SBA must report to the Congress and the President on the agencies' achievements in meeting their small business goals, including those for HUBZone concerns.⁶ This annual report relies on FPDC data.

Reported HUBZone Program Contracting Achievements Are Inaccurate

The data that federal agencies reported on fiscal year 2000 HUBZone contracting achievements is significantly inaccurate. In fact, we identified data inaccuracies that put hundreds of millions of dollars in reported achievements in question. The inaccuracies were due to data entry errors and insufficient guidance for federal contracting personnel on how to complete the forms used to submit data to FPDC. Inaccurate reporting of

⁵ A prospective contractor is considered responsible if it has the capability and financial resources to perform a contract. FAR 9.104-1.

⁶ The Small Business Act, states that SBA shall annually report to the President and the Congress on the extent of participation of small business concerns, including qualified HUBZone small business concerns, in agencies' procurement contracts. The annual report is called *The State of Small Business*. P.L. 100-656, as codified in 15U.S.C. 644(h).

HUBZone achievements limits the ability of federal agencies and the Congress to gauge the success of the program.

For fiscal year 2000, federal agencies reported to FPDC that they awarded 1,803 contracts valued at \$663 million to certified HUBZone firms. However, we found that federal agencies were overcounting some achievements while potentially undercounting others. First, 61 percent of the reported contracts and 53 percent of the reported dollars should not have been reported as fiscal year 2000 HUBZone program achievements. Specifically, we found that federal agencies actually awarded 1,034 of the 1,803 reported HUBZone contracts (with obligations of about \$325 million) to firms not certified to participate in the HUBZone program. Also, we identified another 57 contracts with obligations of about \$24 million that were awarded before the start of the program. Second, when we compared SBA's contractor certification data with FPDC's contracting activity data, we found that federal agencies did not report up to 1,712 contracts—\$589 million—awarded to firms that may have been qualified as HUBZone program participants. However, because FPDC collects only the month and year of contract awards, we could not readily compare a firm's certification date with a specific contract award date. As a result, we could not determine the actual number or value of contracts awarded to HUBZone firms.

We identified problems at the contracting officer level and the agencywide level that contributed to inaccurate data reported to FPDC. FPDC perpetuates these errors by including the inaccuracies in its annual report on federal procurement activities.

- First, contracting officers are not accurately filling out the forms used to report contracting data to FPDC. In some cases, contracting officers simply entered the wrong data when completing the forms. In other cases, contracting officers stated that they were unfamiliar with agency forms and lacked guidance on how to fill them out. Agency forms change regularly to incorporate new reporting requirements or when an agency implements an automated reporting system. Contracting officers receive limited guidance on completing agency forms from an FPDC manual. An FPDC official agreed that the manual does not provide sufficient guidance to preclude errors in overcounting or undercounting achievements. FPDC plans to publish additional guidance to address these inaccuracies before fiscal year 2002.
- Second, agencies are unsure of what qualifies as a HUBZone contract award because SBA did not provide guidance about which contracts to count towards HUBZone program achievements. According to SBA

officials, a contract awarded to a firm that is not certified to participate in the HUBZone program should not count as a HUBZone achievement, regardless of whether the firm became certified during the term of the contract. However, some agencies are counting obligations on multiple year contracts⁷ even though the contract award occurred before the contractors became HUBZone certified. In recent discussions with federal agency officials, SBA officials recognized that for some long-term, multiple year contracts, following SBA's current policy could result in agencies not receiving credit for directing funds to certified HUBZone firms. Consequently, SBA is reviewing its policy on which contract obligations to count towards the HUBZone program.

- Third, FPDC perpetuates inaccurate reporting by publishing reports that contain known errors. FPDC checks agency-provided data to identify apparent inconsistencies, notifies agencies of the errors identified, and requests corrective actions. Agencies took varying degrees of corrective action on errors identified in the preliminary HUBZone data for fiscal year 2000, but they did not correct all the errors that FPDC identified. An FPDC official stated that FPDC does not have the knowledge to correct the data nor the authority to require agencies to correct the data. As a result, the data appears as reported by federal agencies.

SBA relies on FPDC data to report on the HUBZone program to the President and the Congress. SBA's Associate Administrator for the HUBZone program stated that HUBZone information in SBA's fiscal year 2000 report on small business programs will have to include a disclaimer because of data inaccuracies.

Federal Agencies Are Having Difficulty Implementing the HUBZone Program

Despite the inaccuracies in FPDC data, we determined that there are problems implementing the HUBZone program. None of the original ten agencies authorized to implement the program met the fiscal year 2000 statutory goal of awarding 1.5 percent of their prime contract awards to HUBZone firms. Further, one agency awarded only one contract to a HUBZone firm, and another did not award any. Moreover, our analysis of the agencies' contract awards revealed that out of the 10 agencies, 7 used

⁷ Multiple year contracts contain option years beyond a base period that the agencies can exercise so the contractors can continue performing the contract. After the contractors begin performance on the multiple year contract, the SBA may certify the firm as a HUBZone firm. In such cases, when exercising contract options, the agencies are counting the amounts paid to the firm subsequent to certification as HUBZone contract awards.

the HUBZone Act preferences to award only 52 contracts with \$24 million in obligations.

Contracting officers and agency officials confirmed that they are having difficulty implementing the program and cited several reasons for this. First, there is a relatively small number of certified HUBZone firms. We found that in approximately 8,000 HUBZones, SBA had certified 290 firms for participation in the program at the start of fiscal year 2000 and by the end of the fiscal year had certified a total of 1,940 firms nationwide. According to several contracting officers and SBA officials, many small businesses are not aware of the need to apply for certification. To address this problem, SBA officials and agency contracting officers have been informing small businesses about HUBZone program requirements, helping them complete applications to get certified, and holding seminars to encourage more applications. However, while the number of applications to SBA has increased significantly in 2001, the number of certifications has not. As of September 30, 2001, SBA had certified about 4,100 firms.

Second, contracting officers cannot easily locate certified HUBZone firms that provide particular goods and services. Contracting officers told us that they rely on SBA's PRO-Net database as a primary source for identifying potential HUBZone firms. However, sometimes the information the companies enter into the database is not specific or reliable enough to ascertain the firms' capabilities. For example, a General Services Administration contracting officer stated that building mechanical maintenance is a common capability cited by firms listed in PRO-Net, but he had difficulty identifying a company that could perform mechanical maintenance on building elevators. SBA officials stated that they periodically remind the small businesses of the need to regularly update their PRO-Net information so that the database contains the information needed by federal contracting personnel.

Third, SBA instructs agencies in informal guidance to place more emphasis on the 8(a) program than the HUBZone program when federal agencies award contracts to small businesses. Specifically, the SBA guidance ranks the small business programs and places an 8(a) firm that is also a certified HUBZone firm before an 8(a) firm and an 8(a) firm before a

HUBZone firm.⁸ Because several agencies expressed concerns about the perceived lack of flexibility in this order of precedence, SBA is reviewing its guidance in this regard.

Finally, it is easier and quicker for agency officials to award a contract using the 8(a) sole source program. A contracting officer can notify the SBA of the intent to award a sole source contract to an 8(a) firm by providing a brief justification for the selection of the specific 8(a) firm and can negotiate directly with the firm to achieve a fair market contract price. Federal agencies can complete this process in as few as 3 months. In contrast, a contracting officer must determine that only one HUBZone firm exists to perform the work on a sole source contract to a HUBZone firm. Contracting officials can determine this (1) by conducting market research or (2) by having only one responsible firm respond to an announcement for a HUBZone set-aside procurement. A contracting officer stated that completing this process could take as long as a year.

Conclusions

Accurate reporting of HUBZone program information would allow federal officials to better gauge the success of the program. However, the quality of fiscal year 2000 HUBZone contracting data that federal agencies reported to the FPDC was not credible. Without accurate data, the Congress and the President are not able to ensure that the program is working as intended to provide assistance to economically distressed areas of the United States. Most of the reporting errors could have been avoided had contracting personnel had adequate guidance on how to complete the forms submitted to FPDC. Also, some errors could be corrected if the federal agencies and FPDC work together to address the inaccuracies identified in FPDC's review of data.

Further, the ten federal agencies that Congress charged with implementing the program awarded only 52 contracts using HUBZone Act preferences during all of fiscal year 2000. Clearer guidance on how firms should inform agencies about their capabilities would enable contracting officers to more easily locate firms for specific contract opportunities and could increase the number of contracts awarded to certified HUBZone firms using the act's preferences.

⁸ While SBA's regulations (13 CFR 126.607) and the Federal Acquisition Regulation (FAR 19.800(e)) allow contracting officers discretion when deciding whether to use the 8(a) or HUBZone programs, federal agencies usually rely on SBA's informal guidance on the order of precedence when awarding contracts to small businesses.

Recommendations for Executive Action

To improve the accuracy of the data reported by federal agencies, we recommend the Administrator, Office of Federal Procurement Policy, in consultation with SBA when appropriate, strengthen the guidance for all federal agencies about reporting small business program contracting activities to the Federal Procurement Data Center. At a minimum, this guidance should address how the forms should be completed and verified, and clarify how to report which small business preference program was used to award the contract.

To improve the accuracy of data at an agencywide level, we recommend the Administrator of SBA develop guidance for all federal agencies about identifying contracts to be reported to the FPDC that meet the HUBZone Act criteria.

To help ensure that FPDC does not perpetuate data inaccuracies, we also recommend that the Administrator, Office of Federal Procurement Policy, develop follow-up review procedures to emphasize to federal agencies their responsibility in providing accurate data and promptly correcting inaccurate data.

To help contracting officers identify firms with the appropriate capabilities, we also recommend the Administrator of SBA inform small businesses listed in PRO-Net about the importance of entering and maintaining timely, complete, and accurate data.

Agency Comments and Our Evaluation

We received written comments from SBA and oral comments from the Office of Federal Procurement Policy on a draft of this report. SBA generally agreed with our findings and recommendations although SBA had three concerns. First, SBA suggested that the first recommendation be revised to indicate that the Office of Federal Procurement Policy should consult with SBA in developing new guidance. We revised the recommendation accordingly. Second, SBA felt that our report title could be misleading and suggested that our title should be changed to *HUBZone Program Suffers From Procuring Agency Reporting and Implementation Difficulties*. We believe our title appropriately captures the findings of our review, with which SBA agreed; therefore, we did not make this change. Third, SBA took issue with our characterization of the emphasis given to the 8(a) program relative to the HUBZone program. SBA cited a letter the agency sent to Senator Bond dated August 17, 2001, which states that there is parity between the 8(a) program and the HUBZone program, although "regulatory language could be read to give priority to awards to the 8(a) program over HUBZone awards." We noted in our report that

regulations allow contracting officer's discretion in deciding on whether to use the 8(a) or HUBZone programs when awarding contracts. However, SBA's training materials on the HUBZone program, which are given to federal agencies, establish an order of precedence giving the 8(a) program priority over the HUBZone program. As noted in our report and SBA's August 17th letter, SBA is drafting changes to its HUBZone and 8(a) regulations to clarify that contracting officers have discretion to use either program. Therefore, we believe our report accurately reflects SBA's guidance at the time of our review. SBA's comments and enclosure appear in appendix II.

The Office of Federal Procurement Policy generally agreed with our findings. However, based on the Office of Federal Procurement Policy's comments, we revised the recommendation on FPDC reported data to clarify the role that the Office of Federal Procurement Policy should play in ensuring the accuracy of data that agencies provide to FPDC.

Scope and Methodology

To determine whether federal agencies are accurately reporting HUBZone contract achievements, we obtained FPDC's database of all reported obligations to federal government contracts during fiscal year 2000 and SBA's official list of certified HUBZone firms. We reviewed the database and list for three kinds of potential inaccuracies in the FPDC database: (1) contracts reported as HUBZone contracts that were awarded to firms not certified as HUBZone firms, (2) contracts reported as HUBZone contracts that were awarded to firms certified after contract award, and (3) contracts not reported as HUBZone contracts that were awarded to firms that were certified HUBZone firms.

To determine whether federal agencies are having difficulty implementing the HUBZone program to award contracts to certified HUBZone firms, and if so, the reasons for the difficulty, we reviewed the HUBZone Act of 1997 and other pertinent legislation; and HUBZone program implementation guidance contained in Title 13, Code of Federal Regulations (CFR), Part 126 (13 CFR 126), contracting guidance contained in the Federal Acquisition Regulation (48 CFR Chapter 1), and other relevant guidance issued by SBA, FPDC, and the ten program implementing agencies (listed in appendix I). We held discussions about HUBZone program management with officials at the Small Business Administration. We also held discussions with procurement officials at the Small and Disadvantaged Business Utilization Office, and HUBZone program officials at the headquarters level of the ten agencies identified in the HUBZone Act and various field locations of six of those agencies.

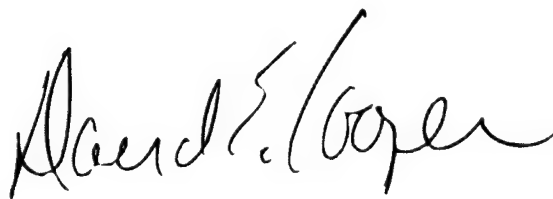
In addition, we determined the extent that agencies used the HUBZone preferences to award contracts. We used FPDC data to identify 136 contracts that the 10 federal agencies reported as being awarded using preferences in fiscal year 2000. We requested relevant contract file information for each of the contracts. We also discussed contract file information with selected contracting officers, who were responsible for 39 of these contracts.

We conducted our review between December 2000 and October 2001 in accordance with generally accepted government auditing standards.

As requested by your office, unless you publicly announce the contents of this report earlier, we plan no further distribution of it until 30 days from the date of this letter. At that time, we will send copies to other interested congressional committees and the secretaries of Defense, Agriculture, Health and Human Services, Transportation, Energy, Housing and Urban Development, and Veterans Affairs. We will send copies to the Director, Office of Management and Budget; the Administrator, General Services Administration; the Administrator, SBA; the Administrator, NASA; the Administrator, EPA; and the Administrator, Office of Federal Procurement Policy. We will also make copies available to others upon request.

Please contact me at (202) 512-4125 or Hilary Sullivan at (214) 777-5652 if you have any questions regarding this report. Major contributors to this report were Frederick G. Day, John E. Clary, and Enemencio S. Sanchez.

Sincerely yours,

A handwritten signature in black ink, reading "David E. Cooper". The signature is fluid and cursive, with the first name "David" being the most prominent.

David E. Cooper
Director
Acquisition and Sourcing Management

Appendix I: Federal Agencies Initially Designated to Implement the HUBZone Program

Agencies designated in the HUBZone Act of 1997 (P.L. 105-135), December 2, 1997:

1. Department of Defense
2. Department of Agriculture
3. Department of Health and Human Services
4. Department of Transportation
5. Department of Energy
6. Department of Housing and Urban Development
7. Department of Veterans Affairs
8. Environmental Protection Agency
9. National Aeronautics and Space Administration
10. General Services Administration

(Each of these ten agencies was included in our review.)

Agencies Added by the Fiscal Year 2000 Appropriation Act (P.L. 106-113), November 29, 1999:

11. Department of Commerce
12. Department of Justice
13. Department of State

(None of these three agencies was included in our review.)

Appendix II: Comments From the Small Business Administration



U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

OCT 15 2001

Mr. David E. Cooper
Director, Acquisition and Sourcing
Management Team
United States General Accounting Office
Washington, DC 20548

Dear Mr. Cooper

Thank you for your letter of September 13, 2001, regarding the General Accounting Office's (GAO) proposed report entitled, "SMALL BUSINESS: HUBZone Program Suffers from Reporting and Implementation Difficulties" (GAO-01-1098). Administrator Barreto has asked me to respond to your report.

The U.S. Small Business Administration (SBA) has reviewed the report and is in general agreement with all findings and recommendations. We find a particular need to ensure that the contract records maintained by the Federal Procurement Data Center (FPDC) on the HUBZone Empowerment Contracting Program, as well as all other small business programs, must be accurate. We agree with the GAO finding that a methodology must be established that allows FPDC to require reporting agencies to correct erroneous data before it is finalized and released to Congress, Administration officials, and the general public. Without accurate data, neither elected officials nor agency program managers can reasonably measure a program's effectiveness or continuing value.

Further, we agree that the FPDC guidance on reporting contract data on small business programs should be strengthened and clarified. Since SBA has oversight responsibility for these programs, we suggest that the first recommendation be revised to indicate that the Office of Federal Procurement Policy should consult with SBA in developing new guidance.

However, we believe that the report's title may be misleading to those only able to scan the document. We feel a more accurate representation of the HUBZone Program's status would be reflected in a title that reads: *HUBZone Program Suffers From Procuring Agency Reporting and Implementation Difficulties*. The reason for this view is based on our assertion that all elements of program development that are within the control of the SBA have been met and, in many cases, exceeded. We have created an online HUBZone application system that forges new ground in customer service via the Internet, conducted a year-long procurement training series that reached an estimated 1,000 Federal contracting officials and certified more than 4,000 small business concerns since starting the process in March 1999.

There are some areas within the control of the SBA that need attention, particularly supplying guidance to agencies for reporting their HUBZone contract accomplishments. We also are aware of the need to stress to registrants in the PRO-Net database the importance of

SBA IS AN EQUAL OPPORTUNITY EMPLOYER AND PROVIDER

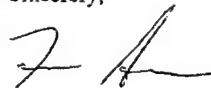
Federal Recycling Program  Printed on Recycled Paper

maintaining current and complete profiles to help contracting officers with source selection. The SBA will meet these challenges and continue working to ensure the success of the HUBZone Program in fulfilling its mission of job creation and capital investment in distressed communities.

Lastly, we note that the report (on pages 8-9) does not properly characterize the interaction between the SBA's 8(a) Business Development program and the HUBZone program. The report states that SBA places more emphasis on the 8(a) program than on the HUBZone program, and instructs agencies to consider the 8(a) program before other programs. In a letter dated August 17, 2001, to Senator Christopher S. Bond, SBA's Acting General Counsel explained SBA's official position regarding the interaction between the 8(a) and HUBZone programs. SBA believes that there is parity between the two programs. In determining which program to use, a contracting officer should consider where the procuring activity is in fulfilling its 8(a) and HUBZone goals, as well as other pertinent factors, and should exercise his or her discretion on whether to use the 8(a) or HUBZone program. I have included a copy of that letter for your review.

If you have any further questions, please call Michael McHale, Associate Administrator for the HUBZone program, at (202) 205-6731.

Sincerely,



Fred C. Armendariz
Associate Deputy Administrator
Office of Government Contracting and
Business Development

Enclosure

Appendix II: Comments From the Small
Business Administration



U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

OFFICE OF GENERAL COUNSEL

August 17, 2001

The Honorable Christopher S. Bond
Ranking Member
Committee on Small Business and Entrepreneurship
United States Senate
Washington, DC 20510

Dear Senator Bond:

Thank you for your letter of July 9, 2001, concerning the Historically Underutilized Business Zone ("HUBZone") program. You have requested an official opinion on the state of the law with respect to concerns eligible for both the HUBZone and 8(a) Business Development ("8(a) BD") programs. I realize that there has been some confusion regarding the interaction between the HUBZone and 8(a) BD programs. With that in mind, I have taken a fresh look at the authority for both programs, and believe that this letter answers all of the questions you have posed.

The six questions you have raised can really be broken down into three issues: (1) the relationship between the 8(a) and HUBZone programs, including your specific concern as to whether contracting officers must attempt to use the 8(a) program before using the HUBZone program; (2) the combined HUBZone 8(a) priority, and its statutory authority; and (3) whether SBA intends to amend its regulations to reflect the interpretation of these programs set forth below.

Relationship between the 8(a) and HUBZone programs

When the U.S. Small Business Administration ("SBA") promulgated its HUBZone regulations, it reviewed all of the provisions of the Small Business Act, including the provisions of the HUBZone program and the provisions of the 8(a) BD program. As you are already aware, the pertinent provision of § 31 of the Small Business Act, which implements the HUBZone program, states:

(2) AUTHORITY OF CONTRACTING OFFICER - Notwithstanding any other provision of law—

* * * *

(B) a contract opportunity shall be awarded pursuant to this section on the basis of competition restricted to qualified HUBZone small business concerns if the contracting officer has a reasonable expectation that not less than 2 qualified

HUBZone small business concerns will submit offers and that the award can be made at a fair market price;

15 U.S.C. § 657a(a). The pertinent provisions of § 8(a) of the Small Business Act, which implement the 8(a) BD program, state that a participant in the 8(a) BD program may receive a sole source award or participate in a procurement restricted, or "set aside," for eligible 8(a) Participants when a requirement is offered to the program. *Id.* §§ 637(a)(1)(D) & (a)(16)(A). In addition, in response to specific Congressional findings,¹ Congress specifically states in the Small Business Act that one of the purposes of the 8(a) BD program is to "expand . . . the procurement by the United States of articles, equipment, supplies, materials, and construction work from small business concerns owned by socially and economically disadvantaged individuals." *Id.* § 631(f)(2)(C) (emphasis added).

The rules of statutory construction require that the various provisions of a single statute be read so that all provisions may have effect and that the statute be a "consistent and harmonious whole." 73 Am. Jur. 2d *Statutes* § 254 at 425 (1974). In addition, although § 31 of the Small Business Act provides that "[n]otwithstanding any other provision of law," the contracting officer ("CO") may award a HUBZone sole source and shall award a HUBZone set-aside if certain requirements are met, courts have held that the phrase "notwithstanding any other provision of law" is not always dispositive. See, e.g., *Oregon Natural Resources Council v. Thomas*, 92 F.3d 792 (9th Cir. 1996) (statutory phrase "notwithstanding any other provision of law" is not always construed literally); *E.P. Paup Co. v. U.S. Dept. of Labor*, 999 F.2d 1341 (9th Cir. 1992) (phrase "notwithstanding any other provision of law" is not necessarily preemptive); *In re The Glacier Bay*, 944 F.2d 577 (9th Cir. 1991) (phrase "notwithstanding the provisions of any other law" was not dispositive of whether that statute implicitly repealed limitation of liability provisions of a different statute). For example, in *Oregon Natural Resources Council*, the court held that the phrase "notwithstanding any other provision of law" was best interpreted as requiring the disregard only of environmental laws and not all applicable laws. *Oregon Natural Resources Council v. Oregon*, 92 F.3d at 796.

¹ With respect to the 8(a) BD program, Congress has found:

- (A) that the opportunity for full participation in our free enterprise system by socially and economically disadvantaged persons is essential if we are to obtain social and economic equality for such persons and improve functioning of our national economy;
- (B) that many such persons are socially disadvantaged because of their identification as members of certain groups that have suffered the effects of discriminatory practices or similar invidious circumstances over which they have no control;
- (C) that such groups include [certain specified groups], and other minorities;
- (D) that it is in the national interest to expeditiously ameliorate the conditions of socially and economically disadvantaged groups;
- (E) that such conditions can be improved by providing the maximum practicable opportunity for the development of small business concerns owned by members of socially and economically disadvantaged groups;
- (F) that such development can be materially advanced through the procurement by the United States of articles, equipment, supplies, services, materials, and construction work from such concerns; and
- (G) that such procurements also benefit the United States by encouraging the expansion of suppliers for such procurements, thereby encouraging competition among such suppliers and promoting economy in such procurements.

Id. § 631(f)(1).

In light of the foregoing, when promulgating the HUBZone regulations, SBA took into consideration the requirement to read the Small Business Act, and all of its provisions, in concert so that it would be a "harmonious whole." Thus, as explained in the preamble to the final HUBZone regulations, "SBA balanced HUBZone contracting with the stated Congressional purpose in the Small Business Act of maximizing 8(a) contracting, where practicable." 63 Fed. Reg. 31896, 31897 (June 11, 1998). In doing so, SBA determined that the phrase "notwithstanding any other provision of law," contained in § 31 of the Small Business Act, is best interpreted as requiring the disregard of provisions of law outside of the Small Business Act and not provisions of law contained within the Small Business Act, such as § 8(a). Accordingly, SBA promulgated the following regulation regarding the award of contracts through the HUBZone program:

When must a contracting officer set aside a requirement for qualified HUBZone SBCs?

- (a) The contracting officer first must review a requirement to determine whether it is excluded from HUBZone contracting pursuant to 126.605.
- (b) The contracting officer must identify qualified HUBZone 8(a) concerns and other 8(a) concerns. The contracting officer must give first priority to qualified HUBZone 8(a) concerns.
- (c) After determining that neither (a) or (b) of this section apply, the contracting officer must set-aside the requirement for competition restricted to qualified HUBZone SBCs if the contracting officer:
 - (1) Has a reasonable expectation, after reviewing SBA's list of qualified HUBZone SBCs that at least two responsible, qualified HUBZone SBCs will submit offers; and
 - (2) Determines that award can be made at a fair and reasonable price.

13 C.F.R. § 126.607.

The regulation itself does not establish an order of precedence between an award under the 8(a) BD program and an award under the HUBZone program.² It requires a CO to identify HUBZone 8(a) and other 8(a) concerns before deciding whether to award through the 8(a) or HUBZone programs, but it does not direct COs to use either program. The only clear priority set forth in the regulations is for "qualified HUBZone 8(a) concerns." I note that the supplementary information to the final rule published in the Federal Register implementing the HUBZone program states that "section [126.607] now establishes a priority first for qualified HUBZone 8(a) concerns and then other 8(a) concerns. After these preferences, the contracting officer must use a HUBZone set-aside competition when possible." 63 Fed. Reg. 31902.

² Moreover, the regulations for both programs recognize that one program should not be used to hurt the other program. As noted in your letter, the HUBZone regulations provide that a contract currently being performed through the 8(a) BD program is not generally available for award through the HUBZone program. 13 C.F.R. § 126.605(b). Similarly, SBA may not accept a requirement for award through the 8(a) BD program if the acceptance would have "an adverse impact on an individual small business, a group of small businesses located in a specific geographical location, or other small business programs, (including the HUBZone program)." 13 C.F.R. § 124.504(c).

It is my view that this supplementary information language is inconsistent with the actual language of the regulation. While the regulatory language could be read to give a priority to awards to the 8(a) program over HUBZone awards, it does not clearly do so. In fact, read in the context of the HUBZone statutory language, I believe that the better interpretation is that this regulation provides for parity between the HUBZone and 8(a) BD programs. A procuring activity CO first identifies qualified HUBZone 8(a) concerns and other 8(a) concerns. Once identified, the CO considers which contracting vehicle is appropriate. In determining which program to use, the CO should consider where the procuring activity is in fulfilling its 8(a) and HUBZone goals, as well as other pertinent factors. The CO is not required, in every instance, to offer the requirement to the 8(a) BD program after identifying eligible 8(a) Participants. Rather, the CO is merely directed to exercise his/her discretion on whether to offer the requirement to the 8(a) BD or HUBZone program.

Priority for Qualified HUBZone 8(a) Concerns

There also has been confusion regarding the priority for "qualified HUBZone 8(a) concerns." In response to your specific question, there is no statutory authority to create a set-aside program reserved exclusively for HUBZone 8(a) concerns. The 8(a) regulations permit SBA to limit competitive 8(a) construction procurements to 8(a) Participants located in specified geographic areas, and permit a procuring activity CO to do the same for non-construction procurements if the solicitation imposes a geographic restriction. 13 C.F.R. §§ 124.507(c)(2) & (3). This is a geographic restriction, not a type of business restriction. As such, SBA or a procuring activity CO could restrict an 8(a) competition to 8(a) Participants located in a specific geographic area which is a HUBZone. This provision could not be used, however, to authorize SBA or the procuring activity CO to restrict an 8(a) competitive requirement to qualified HUBZone concerns. Thus, if an 8(a) competitive procurement were restricted geographically to a HUBZone area, any 8(a) firm having a bona fide place of business in the HUBZone area would be eligible for the procurement, whether or not the firm was also certified as a HUBZone small business. Moreover, the "bona fide place of business" language of the 8(a) regulations has a different meaning than the "principal office" language contained in the HUBZone regulations, so that an 8(a) firm that has a bona fide place of business in a HUBZone may not qualify for the HUBZone program if its principal office is not also located in a HUBZone. As far as giving some sort of preference for 8(a) Participants in the award of HUBZone contracts, there is nothing in the HUBZone regulations which would permit any kind of restricted competition among some (i.e., HUBZone concerns that are also 8(a) Participants), but not all, certified HUBZone concerns.

Moreover, in my view, the Small Business Act does not provide authority to SBA to create a competitive HUBZone/8(a) set-aside, or any kind of price evaluation preference or evaluation credit for a concern that is certified into both the 8(a) BD and HUBZone Programs. I believe that requiring an evaluation preference for an 8(a) HUBZone small business concern in the award of either an 8(a) or HUBZone contract would subject SBA to litigative risk as beyond SBA's statutory authority. The only way for such a priority to have any real meaning would be for Congress to specifically provide for the priority in statute, describing its parameters, so that SBA could promulgate a regulation further assisting those concerns certified into both programs.

That being said, I believe that the Small Business Act and the implementing regulations can reasonably be interpreted to provide a preference for HUBZone 8(a) concerns in one limited circumstance. Pursuant to 13 C.F.R. § 124.502(b)(1), a CO may offer an open requirement to the 8(a) BD program. An open requirement is one in which the procuring activity does not nominate a particular concern for performance of a sole source 8(a) contract, but, rather, offers the requirement to the program generally. 13 C.F.R. § 124.503(d). If the procurement is a construction requirement, SBA examines the portfolio of 8(a) Participants that have a bona fide place of business within the geographical boundaries served by the SBA district office where the work is to be performed to select a qualified participant. *Id.* § 124.503(d)(1). If none are found to be qualified, or a match for a concern in that district is determined to be impossible or inappropriate, SBA may nominate a Participant with a bona fide place of business within the geographical boundaries served by another district office within the same state, or may nominate a Participant having a bona fide place of business out of state, but within a reasonable proximity to the work site. *Id.* If the open requirement is not a construction requirement, SBA may select any eligible, responsible Participant nationally to perform the contract. *Id.* § 124.503(d)(2). In cases in which SBA selects a Participant for possible award from among two or more eligible and qualified Participants, the selection will be based upon relevant factors, including, but not limited to, business development needs, compliance with competitive business mix requirements, financial condition, management ability, technical capability, and whether the award will promote the equitable distribution of 8(a) contracts. *Id.* 124.503(d)(3).

As noted above, SBA has read the statutory provisions of the Small Business Act, including the provisions of the 8(a) BD Program and HUBZone Program, in conjunction with one another. Likewise, SBA reads the various sections of its regulations in conjunction with one another. Thus, § 124.503, concerning open requirements in the 8(a) BD Program, must be read in conjunction with § 126.607. Consequently, with respect to an open requirement, SBA may nominate a qualified HUBZone 8(a) small business concern over another 8(a) Participant, assuming all of the above requirements are met.

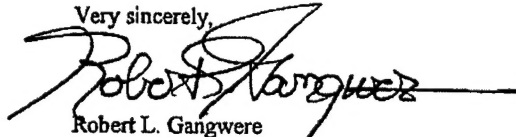
Changes to SBA's Regulations

SBA is committed to making the HUBZone program a success. In furtherance of that goal, SBA is currently in the process of drafting proposed changes to clarify our HUBZone and 8(a) BD regulations with respect to the issues presented in your letter, as well as other programmatic issues. SBA intends to propose amendments to both the HUBZone and 8(a) BD regulations to clarify that a CO has discretion to use either of the two programs, depending on the procuring activity's achievement of goals and other factors. Once any changes in SBA's regulations are finalized, there would also need to be conforming amendments to the Federal Acquisition Regulation.

To ensure that the Agency fully addresses your concerns, we would like to meet with you or a member of your staff to discuss this issue further. We will be contacting your office soon to make arrangements for such a meeting.

As always, we appreciate your input and support. Please feel free to contact me at (202) 205-6642, or John Klein, Associate General Counsel for Procurement Law, at (202) 619-1772, if you need further assistance.

Very sincerely,



Robert L. Gangwere
Acting General Counsel

Ordering Information

The first copy of each GAO report is free. Additional copies of reports are \$2 each. A check or money order should be made out to the Superintendent of Documents. VISA and MasterCard credit cards are also accepted.

Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.

Orders by mail:

U.S. General Accounting Office
P.O. Box 37050
Washington, DC 20013

Orders by visiting:

Room 1100
700 4th St., NW (corner of 4th and G Sts. NW)
Washington, DC 20013

Orders by phone:

(202) 512-6000
fax: (202) 512-6061
TDD (202) 512-2537

Each day, GAO issues a list of newly available reports and testimony. To receive facsimile copies of the daily list or any list from the past 30 days, please call (202) 512-6000 using a touchtone phone. A recorded menu will provide information on how to obtain these lists.

Orders by Internet

For information on how to access GAO reports on the Internet, send an e-mail message with "info" in the body to:

Info@www.gao.gov

or visit GAO's World Wide Web home page at:

<http://www.gao.gov>

To Report Fraud, Waste, and Abuse in Federal Programs

Contact one:

- Web site: <http://www.gao.gov/fraudnet/fraudnet.htm>
- E-mail: fraudnet@gao.gov
- 1-800-424-5454 (automated answering system)

United States
General Accounting Office
Washington, D.C. 20548-0001

Presorted Standard
Postage & Fees Paid
GAO
Permit No. G100

Official Business
Penalty for Private Use \$300

Address Correction Requested

99440810/GAO-02-57 M/001 US

Defense Technical Information
8725 John J Kingman Rd Rm 944
Fort Belvoir VA 22060-6218